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SUBJECT: EU STRATEGY FOR THE SOUTHERN GAS CORRIDOR

¶1. (SBU) Summary. In an April 7 meeting, EU Commission officials discussed the EU's strategy for the Southern Gas Corridor to bring gas from the Caspian region to Europe. Jozias Van Aartsen, the EU's Coordinator for the Southern Gas Corridor, believes the EU and Turkey need to agree to prioritize the Nabucco pipeline project over the other contenders. Nabucco would supply Caspian gas into the Russian dominated market where it would be competition for Russian gas. The Commission reasons that there is enough gas in the Caspian region only for one pipeline to Europe to be built within the next 6-7 years. Van Aartsen plans to lobby EU Commission President Barosso to make Nabucco the EU priority and encourage him to push Turkey to do the same when Barosso visits Turkey on April 11. End Summary.

¶2. (SBU) On April 7 2008 EST Officers met with EU Commission officials to discuss the EU's strategy for the Southern Gas Corridor to bring gas from the Caspian and Middle East to Europe. Brendan Devlin, assistant to Jozias Van Aartsen who is the EU's Coordinator for the Southern Gas Corridor, began by explaining the nature of Mr. Van Aartsen's role in determining EU policy and negotiating on behalf of the EU. Van Aartsen's role is as a facilitator who seeks to guide the negotiations and focus the EU's policy goals. Devlin was keen to point out that Van Aartsen's statements do not necessarily reflect the views of the Commission. Van Aartsen has a wide mandate to push development of the Southern Corridor, while at the same time giving the Commission a certain degree of deniability. Van Aartsen can be contradicted by EU officials and to a certain degree is considered expendable. However, a Commission official who attended the meeting indicated that the Commission is largely in line with Van Aartsen's views.

Van Aartsen's Message to Barosso

¶2. (SBU) Van Aartsen planned to brief EU Commission President Barosso on 8 April on how he thinks the EU should approach the Southern Corridor in advance of Barosso's planned meeting on 11 April with Turkish Prime Minister Erdogan. According to Devlin, Van Aartsen will stress five points with Barosso:

-- The intergovernmental agreement (IGA) for the Nabucco pipeline should be signed in an inter-governmental commission in The Hague in June.

-- Turkey should commit to sending a Vice President for the

IGA ceremony.

-- Azerbaijan and Georgia must take part in the IGA.

-- The EU should offer to cooperate with Turkey on the Turkish domestic gas market.

-- The EU and Turkey should agree that Nabucco is the priority pipeline for both Europe and Turkey. This means prioritizing Nabucco over other competing pipelines such as the Turkey-Greece-Italy (TGI) pipeline and the Trans-Adriatic pipeline (TAP).

Two Separate Agreements Needed for Nabucco

13. (SBU) Devlin indicated that to accomplish Nabucco, two separate agreements would be needed. The first step is the IGA for the entire route with all the countries involved (Azerbaijan, Georgia, Turkey, Bulgaria, Romania, Hungary, Austria.) The IGA would cover taxes, right of ways, jurisdiction, etc., but not transmission. Secondly, Nabucco will need a transmission agreement between the EU and Turkey.

The IGA falls under the competence of the EU Member States involved, but transmission is an EU competence. Such an EU-Turkey transmission agreement would cover all pipelines (Nabucco, TAP, TGI, etc.). Devlin indicated that TGI broke EU rules when it included netback terms in the TGI pipeline IGA. This should have been handled via an EU-Turkey agreement because transmission is an EU competence.

14. (SBU) Van Aartsen has been encouraging Turkey to sign on to the Energy Community Treaty so that Turkey can use the treaty for the transmission agreement. Turkey is an observer of the Treaty, but not a signatory. Devlin indicated the

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Energy Community Treaty basically applies EU rules and would require that transmission fees be directly related to costs. The alternative to using the treaty would be to negotiate an EU-Turkey bilateral transmission agreement from scratch. Van Aartsen is arguing against the bilateral approach because negotiating such an agreement would inevitably bring up Turkish accession to the EU, Cyprus, and other political issues. One Member State could potentially block it. Devlin pointed out that negotiating the Energy Community Treaty took six years and negotiating a bilateral EU-Turkey transmission treaty from scratch could equally delay Nabucco by six years or more (especially with Italy likely to delay so that they can get TGI first). Van Aartsen has offered Turkey the option of deleting the parts of the Energy Community Treaty they don't like (coal fired power plant restrictions, targets on sulfur, etc.) as long as they keep the relevant sections on transit.

15. (SBU) Turkey has consistently said no to the Energy Community idea, but the reasons for their opposition may be misunderstanding of the treaty. Devlin opined that at a working level the Turks do not see the opportunities the treaty would provide; only the perceived restrictions it would impose. He believes the EU needs to educate working level Turkish authorities on the possibilities presented by the treaty and the art of "imaginative implementation" as practiced by the EU member states.

Why Nabucco?

16. (SBU) In response to EST officer's questions on why Nabucco should be the priority and not TGI or TAP or any of the other projects, Devlin responded that the Nabucco pipeline has the highest strategic importance for the EU. Nabucco is the biggest project (31 bcm/y) whereas the TGI is only 8 bcm/y. Nabucco would supply Caspian gas into the Russian dominated market where it would be competition for Russian gas and provide an alternative supplier to countries which only have one choice - Russia. A pipeline into Italy, where it would compete with Algerian gas, would not have the

same strategic importance, he said. TGI gas won't get out of the Italian market. The White Stream project would also be a viable project and has several advantages, but the project is not very far along and Nabucco is much further advanced. Van Aartsen believes there is not enough gas for all the pipeline projects at once. If TGI goes first it would suck up the gas for Nabucco and delay Nabucco by as much as five years. Nabucco would provide the strategic benefit of countering Russian market dominance. And with Nabucco, gas could still flow to Italy via the hub in Baumgarten.

Timing Matters

17. (SBU) Devlin stressed that timing is critical for the Nabucco project. This summer a number of long-term gas contracts in member states will come up for renewal, notably in Hungary. Negotiations for these supply contracts will be ongoing through the fall. Devlin opined that if companies have a 99 percent guarantee of Nabucco gas and 100 percent guarantee of Russian gas they will opt for Russian gas. He stressed that the supply gap is now. He believes the member states need a viable alternative to Russian gas by the end of the year. If Nabucco doesn't get this batch of contracts they'll have to rebuild the supply contracts over time, which could delay Nabucco's startup until 2017. To make Nabucco a viable alternative to Russian gas, Van Aartsen believes the EU needs to remove the risk from the equation. As such, Van Aartsen is looking at possible European Investment Bank mechanisms to remove the risk for suppliers and consumers such as "Off take or Pay" guarantees for suppliers (Azerbaijan, Turkmenistan, etc.) and "Ship or Pay" guarantees for consumers.

18. (SBU) Van Aartsen is hoping to wrap up the EU-Turkey transmission agreement by September or November. The EU wants to have a final investment decision on Nabucco during the French Presidency. The EU also wants to get a Turkish agreement on Gaz de France (GDF) participation in Nabucco. Turkey originally said they excluded GDF on technical grounds, but later leaked that they did it for political reasons. Van Aartsen believes French support for the project is crucial. Van Aartsen is not planning to go to Azerbaijan

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or Turkmenistan until he has a "cash deal" he can lay on the table. His philosophy is he should hold back until he has a concrete deal to offer. In Van Aartsen's opinion, according to Devlin, too many people have been going to Azerbaijan and Turkmenistan, saying "this is really important", and then going away again. When Van Aartsen goes, he wants to be able offer a fixed route and an investment guarantee. The next technical meeting with Turkey will be in Istanbul on April 21, 2008.

The USG Role

19. (SBU) As for what the USG can do to support the EU's efforts Gas for Nabucco Devlin requested two things: 1.) Encourage Georgia and Azerbaijan to participate in the discussions on transmission and 2.) Get Turkey to propose to prioritize Nabucco over the other options. Devlin also suggested the US could play a role in educating Turkish officials on the concept of a commercial gas hub. The EU is not opposed to Turkey having a commercial gas hub, like an EU or a US commercial gas hub -- Not acting as an intermediary, just a market place, with an operator running things. Turkey, on the other hand, has been pushing the idea of the hub acting as an intermediary. Devlin jokingly suggested flying the staff from Henry Hub to Turkey to teach them how a commercial hub works. The EU is trying to get Turkey to give up the idea of being the "Ukraine of the South."

110. (SBU) Comment. Van Aartsen's priorities are not necessarily the Commission's priorities, but they are probably close. And Barroso could in the near term wind up adopting Van Aartsen's objectives. The Commission has trouble

promoting one pipeline over another, because each of the proposed pipelines would benefit various member states. End Comment.

Murray

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